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TAGS: [ETRD](#) [ELAB](#) [PGOV](#) [SENV](#) [CA](#)

SUBJECT: Strong Loonie - Cross-border Shopping Hurts Canadian Auto Producers

Ref: (A) Toronto 450 (B) Toronto 414 (C) Toronto 358 (D) Toronto 53

(E) Toronto 11

Sensitive But Unclassified - Please Protect Accordingly.

11. (SBU) Summary: The strong Canadian dollar and weaker U.S. consumer demand are challenging Canadian-based auto assemblers' efforts to remain globally competitive. Sales to Canadians of new and used autos from the U.S. are up by 21% to 136,666, setting a new record for the first 10 months of the year. The auto parts sector is asking the Ontario provincial and Canadian federal governments for assistance to stay afloat. Ford Canada has condemned the pending Canadian -- South Korean Free Trade Agreement. The auto sector employs more than 130,000 people in Ontario, and represents a large portion of the manufacturing sector (20% of provincial GDP). We believe provincial officials will continue their efforts to help auto companies adapt to the challenging economic reality of a strong Canadian dollar and weaker U.S. consumer demand. Provincial efforts to persuade the Conservative federal government to help the sector may be less immediately successful. End Summary.

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Canadians Importing More Cars from the U.S.  
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12. (SBU) The strong Canadian dollar and resulting lower auto sticker price has prompted Canadians to import more cars from the U.S. and buy fewer cars in Canada. Vehicle sales in Canada dropped 3% in September to 132,165 vehicles from 136,057 in the same period last year, only to show a slight recovery in October (ref (A)). The Bank of Montreal recently estimated that the price of Canadian goods is roughly 25% higher than in the U.S.

13. (SBU) Imports of new and used autos from the U.S. are up a record 21% to 136,666 cars for the first 10 months of the year compared to the same period last year, according to the federal Registrar of Imported Vehicles. In October, a month after the Canadian dollar surpassed the U.S. dollar for the first time in more than 30 years, auto imports doubled over the same period last year. Ontario and B.C. accounted for two thirds of overall imports this year, which is proportionately higher than in past years. The industry has responded to the surge in imports by introducing incentives to reduce new car prices in Canada by roughly 5%.

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Auto Parts Sector Asking for Government Bail Out  
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14. (SBU) Canada's auto parts suppliers, led by Gerry Fedchun,

President of the Canadian Automotive Parts Manufacturers' Association (APMA), have asked the Canadian federal and Ontario provincial governments for C\$400 million in "emergency" financing to help survive the surge in the Canadian dollar. Canadian auto parts makers employ about 90,000 people, primarily in Ontario and Quebec, and manufacture more than C\$30 billion worth of goods and services annually.

15. (SBU) Many parts manufacturers have already been forced to cut jobs or close plants because of declining production at their largest customers, the Detroit Three -- GM, Ford, and Chrysler. The auto parts makers have been squeezed by production cuts and shrinking margins as the Detroit Three demand price cuts from their suppliers while commodity input prices, such as steel and plastic have been increasing. The APMA says it would direct the C\$400 million in loans for new equipment purchases to improve the productivity of smaller member companies. Larger players like Aurora, Ontario-based Magna and Guelph, Ontario-based Linamar have capitalized on the rising Canadian dollar (from US\$0.85 to more than US\$1.00 in seven months) to purchase and install new equipment to boost productivity. Smaller companies lacked the margin to take advantage of the stronger Canadian dollar.

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Ford Condemns Proposed Canada-Korea FTA  
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16. (SBU) On November 22 at the Economic Club of Toronto, Ford Canada President Bill Osborne joined other Canadian auto manufacturers and the Canadian Auto Workers union in criticizing a pending free trade agreement between Canada and South Korea. Osborne said a Canada-South Korea free trade agreement that does not include more open access to the Korean auto market would make it difficult for Ford to justify making more investments in Canada. He warned that,

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if Canadian negotiators emulate the proposed U.S.-South Korea deal, which would reportedly end the U.S. tariff on small Korean cars, it could result in "serious economic harm" to Canadian auto manufacturers. Because Canada's market is more heavily skewed to compact cars than the U.S. market, he argued, Canadian auto manufacturers would be harder hit by a trade agreement that does not effectively open Korean markets to North American autos.

17. (SBU) Comment: On November 27 Ontario Premier Dalton McGuinty reportedly said the federal government should sit down with provincial officials and auto industry leaders to decide how to help the struggling sector. Citing federal funding of infrastructure projects, work to harmonize fuel efficiency standards with the U.S., elimination of the federal capital tax, accelerated capital cost allowances for manufacturers, and a federal corporate tax rate cut, federal officials reacted coolly to the suggested talks. Ontario claims its C\$500 million five-year Automotive Investment strategy, announced in April 2004, has so far resulted in C\$7 billion of net new investment and creation of 7,000 new jobs. Because the auto sector employs more than 130,000 people in Ontario, and represents a large portion of the manufacturing sector (20% of provincial GDP), we believe the provincial government will actively intervene to help the auto sector in the coming months as small to medium-sized companies continue their efforts to stay afloat with small or non-existent profit margins. Provincial officials are also likely to continue seeking assistance from the federal government, though the Conservative federal government is ideologically inclined toward broadly-based tax relief, rather than subsidies, and is likely to delay any such measures until the announcement of its FY08-09 budget (February 2008 at the earliest). End Comment.

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